

# Referral Matters

## Part IV

### Findings and Recommendations

#### Failure to Respond to the Interim Audit Report

An interim audit report was issued on March 21, 2008, advising DSC of the findings and recommendations resulting from the audit of the Derrick Shepherd Campaign Committee. The Audit staff contacted the treasurer on March 28, 2008 to confirm receipt of the interim audit report. DSC was requested to respond to the interim audit report by April 23, 2008. On April 22, 2008 the treasurer was sent an e-mail reminding him of the response due date. DSC did not respond to the interim audit report nor request an extension of time to respond.

#### Finding 1. Permissibility of Candidate Loans

##### Summary

DSC reported twelve loans from the Candidate totaling \$154,125. The Audit staff made numerous requests of DSC for supporting documentation to determine whether the loans were made from the Candidate's personal funds. In addition, a letter was sent to the Candidate requesting such documentation which was followed by a telephone conversation concerning the needed records. No documentation has been provided. The Audit staff recommended that DSC provide evidence demonstrating that these loans were made from the Candidate's personal funds.

##### Legal Standard

**A. Formal Requirements Regarding Reports and Statements:** An authorized committee shall maintain all records, including bank records, with respect to the matters required to be reported which shall provide in sufficient detail the necessary information and data from which the filed reports and statements may be verified, explained, clarified, and checked for accuracy and completeness. 11 CFR §104.14(b)(1).

**B. Expenditures by Candidates.** Candidates for Federal office may make unlimited expenditures from personal funds as defined in 11 CFR §§100.33 and 110.10.

**C. Personal Funds.** Personal funds of a candidate means the sum of all of the following:

1. **Assets.** Amounts derived from any asset that, under applicable State law, at the time the individual became a candidate, the candidate had legal right of access to or control over, and with respect to which the candidate had-
  - Legal and rightful title; or
  - An equitable interest;
2. **Income.** Income received during the current election cycle, as defined in 11 CFR 400.2, of the candidate.

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3. **Jointly owned assets.** Amounts derived from a portion of assets that are owned jointly by the candidate and the candidate's spouse as follows:
- The portion of assets that is equal to the candidate's share of the asset under the instrument of conveyance or ownership; provided, however,
  - If no specific share is indicated by an instrument of conveyance or ownership, the value of one-half of the property. 11 CFR §100.33.

### **Facts and Analysis**

DSC reported receiving twelve loans from the Candidate totaling \$154,125.<sup>1</sup> For \$141,500 of these loans, DSC provided copies of checks drawn on the Candidate's personal bank accounts used to make these loans. In addition, DSC provided copies of money orders purchased by the Candidate to make \$10,000 of these loans and a certified bank check used to make another \$1,625 loan. For the remaining loans (\$1,625), DSC only provided copies of deposit slips which indicated checks were deposited; however, the check copies were not made available.

In order to verify that the source of funds for all of these loans was the Candidate's personal funds, it is necessary for the Audit staff to review, at a minimum, the records for the accounts that the checks were drawn on, and documentation to verify the source of the funds used to purchase the cashier's check and money orders. The Audit staff made numerous requests of DSC for this documentation, but none was provided. In addition, a letter was sent to the Candidate requesting such documentation and noting that if not provided the Commission may draw an adverse inference about the source of the funds from the failure to provide the requested records. Finally, a follow-up telephone conversation was held with the Candidate to reiterate the need for these records. None of the documentation requested has been provided by either DSC or the Candidate.

At the exit conference, the Audit staff discussed this issue with DSC's representative and a schedule was provided detailing the loan activity.

### **Interim Audit Report Recommendation**

The Audit staff recommended that, within 30 calendar days of service of the interim report, DSC provide evidence demonstrating that the loans to DSC were made from the Candidate's personal funds. It was noted that failure to provide the necessary records may lead the Commission to draw an adverse inference concerning the source of the funds provided to DSC by the Candidate.

## **Finding 2. Receipt of Prohibited Contributions**

### **Summary**

DSC received sixteen prohibited contributions totaling \$22,900 from limited liability companies (LLCs) and corporate entities. Should DSC establish that the contributions from two of the limited liability companies are from permissible sources, \$7,200 would

<sup>1</sup> The 2007 April 15 Quarterly report filed by DSC converts these loans to contributions from the Candidate and distinguishes the loans.

be added to the excessive contributions in Finding 3. Of this amount, \$4,200 could be resolved by DSC sending presumptive refundation letters. The remaining excessive contributions totaling \$3,040 are resolvable only by means. The Audit staff recommended that DSC either provide evidence that these contributions were made with permissible funds or refund them.

### **Legal Standard**

**A. Receipt of Prohibited Corporate Contributions.** Political campaigns may not accept contributions made from the general treasury funds of corporations. This prohibition applies to any type of corporation including a non-stock corporation, an incorporated membership organization, and an incorporated cooperative. 2 U.S.C. §441b.

**B. Definition of Limited Liability Company.** A limited liability company (LLC) is a business entity recognized as an LLC under the laws of the state in which it was established. 11 CFR §110.1(g)(1).

**C. Application of Limits and Prohibitions to LLC Contributions.** A contribution from an LLC is subject to contribution limits and prohibitions, depending on several factors, as explained below:

1. **LLC as Partnership.** The contribution is considered a contribution from a partnership if the LLC chooses to be treated as a partnership under Internal Revenue Service (IRS) tax rules, or if it makes no choice at all about its tax status. For the 2006 election, a partnership contribution may not exceed \$2,169 per candidate, per election, and it must be attributed to one or more partners. 11 CFR §110.1(a), (b), (e) and (g)(2).
2. **LLC as Corporation.** The contribution is considered a corporate contribution—and is barred under the Act—if the LLC chooses to be treated as a corporation under IRS rules, or if its shares are traded publicly. 11 CFR §110.1(g)(3).
3. **LLC with Single Member.** The contribution is considered a contribution from a single individual if the LLC is a single-member LLC that has not chosen to be treated as a corporation under IRS rules. 11 CFR §110.1(g)(4).

**D. Limited Liability Company's Responsibility to Notify Recipient Committee.** At the time it makes a contribution, an LLC must notify the recipient committee:

- That it is eligible to make the contribution; and
- In the case of an LLC that considers itself a partnership (for tax purposes), how the contribution should be attributed among the LLC's members. 11 CFR §110.1(g)(5).

**E. Questionable Contributions.** If a committee receives a contribution that appears to be prohibited (a questionable contribution), it must follow the procedures below:

1. Within 18 days after the treasurer receives the questionable contribution, the committee must either:
  - Return the contribution to the contributor without depositing it; or
  - Deposit the contribution (and follow the steps below). 11 CFR §103.3(b)(1).
2. If the committee deposits the questionable contribution, it may not spend the funds and must be prepared to refund them. It must therefore maintain sufficient

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funds to make the refunds or establish a separate account in a campaign depository for possibly illegal contributions. 11 CFR §103.3(b)(4).

3. The committee must keep a written record explaining why the contribution may be prohibited and must include this information when reporting the receipt of the contribution. 11 CFR §103.3(b)(5).
4. Within 30 days of the treasurer's receipt of the questionable contribution, the committee must make at least one written or oral request for evidence that the contribution is legal. Evidence of legality includes, for example, a written statement from the contributor explaining why the contribution is legal or an oral explanation that is recorded by the committee in a memorandum. 11 CFR §103.3(b)(1).
5. Within those 30 days, the committee must either:
  - Confirm the legality of the contribution; or
  - Refund the contribution to the contributor and note the refund on the report covering the period in which the refund was made. 11 CFR §103.3(b)(1).

**F. Refund or Discharge Questionable Contributions.** If the identity of the original contributor is known, the committee must either refund the funds to the source of the original contribution or pay the funds to the U.S. Treasury. AO 1996-5.

#### **Facts and Analysis**

A review of contributions from individuals resulted in the identification of 16 apparent prohibited contributions totaling \$22,900. Of these, 14 contributions totaling \$22,600 had been received from ten LLCs. DSC did not provide documentation detailing the tax filing status of these entities. The two remaining contributions totaling \$300 were from entities whose corporate status was verified with the Secretary of State. DSC did not maintain sufficient funds in its bank account to make the necessary refunds.

Should DSC establish that the contributions from two of the limited liability companies are from permissible sources, \$7,200 would be added to the excessive contributions in Finding 3. Of this amount, \$4,200 could be resolved by DSC sending pre-nuptive redesignation letters. The remaining excessive contributions totaling \$3,000 are resolvable only by refund.

At the exit conference, the Audit staff discussed this issue with DSC's representative and provided schedules. The representative agreed to review these schedules to determine whether they concurred with the exceptions listed and respond accordingly.

#### **Interim Audit Report Recommendation**

The Audit staff recommended that, within 30 calendar days of service of the interim report, DSC:

- Provide evidence demonstrating that the contributions in question were made with permissible funds and were not excessive; or
- Refund the impermissible funds, refund/resolve the excessive contributions as noted above and provide evidence of such refunds (copies of the front and back of negotiated refund checks) or disgorge the funds to the U.S. Treasury; or

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- If funds are not available to make the necessary refunds, disclose the contributions requiring refunds on Schedule D (Debt and Obligations) until funds become available to make such refunds.

### **Finding 3. Receipt of Contributions that Exceed Limits**

#### **Summary**

DSC accepted 36 contributions from individuals that exceeded the limit by \$61,310. Of these excessive contributions, \$31,310 was eligible for presumptive election designation and contributor attribution. However, there was no evidence that the required notices had been sent to contributors. The remaining excessive contributions, \$30,000, were not eligible for presumptive redesignation and/or reattribution. The Audit staff recommended that DSC provide evidence demonstrating that the contributions were not excessive, send notices to those contributors that were eligible for presumptive redesignation and/or reattribution, or refund the excessive amounts.

#### **Legal Standard**

**A. Authorized Committee Limits.** For the 2006 election, an authorized committee may not receive more than a total of \$2,100 per election from any one person as adjusted by the Consumer Price Index (CPI). 2 U.S.C. §441a(a)(1)(A), (2)(A) and (f); 11 CFR §§110.1(a) and (b) and 110.9(a).

**B. Handling Contributions That Appear Excessive.** If a committee receives a contribution that appears to be excessive, the committee must either:

- Return the questionable contribution to the donor; or
- Deposit the contribution into its federal account and keep enough money on account to cover all potential refunds until the legality of the contribution is established. 11 CFR §103.3(b)(3) and (4).

The excessive portion of contributions may also be redesignated to another election or reattributed to another contributor as explained below.

**C. Redesignation of Excessive Contributions.** The committee may ask the contributor to redesignate the excess portion of the contribution for use in another election.

- The committee must, within 60 days of receipt of the contribution, obtain and retain a signed redesignation letter which informs the contributor that a refund of the excessive portion may be requested; or
- Refund the excessive amount. 11 CFR §§110.1(b)(5), 110.1(l)(2) and 103.3(b)(3).

Notwithstanding the above, when an authorized political committee receives an excessive contribution from an individual or a non-auxiliary committee, the committee may presumptively redesignate the excessive portion to the general election if the contribution:

- Is made before that candidate's primary election;
- Is not designated in writing for a particular election;

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- Would be excessive if treated as a primary election contribution; and
- As redesignated, does not cause the contributor to exceed any other contribution limit.

Also, the committee may presumptively redesignate the excessive portion of a general election contribution back to the primary election if the amount redesignated does not exceed the committee's primary net debt position.

The committee is required to notify the contributor in writing of the redesignation within 60 days of the treasurer's receipt of the contribution and must offer the contributor the option to receive a refund instead. For this action to be valid, the committee must retain copies of the notices sent. Presumptive redesignations apply only within the same election cycle. 11 CFR §110.1(h)(5)(ii)(B) & (C) and §110.1(i)(4)(ii).

**D. Reattribution of Excessive Contributions.** When an authorized committee receives an excessive contribution, the committee may ask the contributor if the contribution was intended to be a joint contribution from more than one person.

- The committee must, within 60 days of receipt of the contribution, obtain and retain a reattribution letter signed by all contributors; or
- Refund the excessive contribution. 11 CFR §§110.1(k)(3), 110.1(l)(3) and 103.3(b)(5).

Notwithstanding the above, any excessive contribution that was made on a written instrument that is imprinted with the names of more than one individual may be attributed among the individuals listed unless instructed otherwise by the contributor(s). The committee must inform each contributor:

- How the contribution was attributed; and
- The contributor may instead request a refund of the excessive amount. 11 CFR §110.1(k)(3)(ii)(B).

For this action to be valid, the committee must retain copies of the notices sent. 11 CFR §110.1(l)(4)(ii).

**E. Refund or Disgorge Questionable Contributions.** If the identity of the original contributor is known, the committee must either refund the funds to the source of the original contribution or pay the funds to the U.S. Treasury. AO 1996-5.

### **Facts and Analysis**

The Audit staff reviewed contributions from individuals to determine if excessive contributions were received. The review identified 36 contributions that exceeded the limit by \$61,310. During this review, it was noted that DSC routinely redesignated contributions to another election or reattributed contributions to another individual. However, no documentation was provided by DSC in support of these redesignations and reattributions; neither signed redesignations or reattributions, nor the contribution notifications required for presumptive reattribution or redesignation.

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Of the excessive contributions, \$31,310 could be resolved by DSC sending presumptive redesignation and/or reattribution letters. The remaining excessive contributions totaling \$30,000 are resolvable only by refund. DSC did not maintain sufficient funds in its bank account to make the necessary refunds.

At the exit conference, the Audit staff provided DSC's representative with schedules of the excessive contributions noted above. The representative agreed to review these schedules to determine whether he concurred with the exceptions listed and would respond accordingly.

#### **Interim Audit Report Recommendation**

The Audit staff recommended that, within 30 calendar days of service of the interim report, DSC:

- Send notices to those contributors whose contributions were eligible for presumptive redesignation and/or reattribution (\$31,310) informing them how their contribution was designated and/or attributed and offer a refund of the excessive amount. Absent a request for a refund by the contributors, these notices would obviate the need for contribution refunds or payments to the U.S. Treasury. For notices sent to contributors, DSC should provide a copy of each notice and evidence that it was sent. The notices must demonstrate that both the contributor and the individual to whom the contribution was reattributed were notified. If any contributor cannot be located or if the presumptive notice comes back undeliverable, a disgorgement of the excessive contribution should be made to the U.S. Treasury; and
- Provide evidence demonstrating that the remaining contributions totaling \$30,000 were not excessive. Such evidence should include, but not be limited to, documentation that the contributions were reattributed, redesignated, or refunded in a timely manner; or
- Absent such evidence, refund \$30,000 to the contributors and provide evidence of such action (copies of the front and back of negotiated refund checks) or make a disgorgement to the U.S. Treasury; or
- If funds are not available to make the necessary refunds, disclose the contributions requiring refunds on Schedule D (Debt and Obligations) until funds become available to make such refunds.

#### **Finding 4. Misstatement of Financial Activity**

##### **Summary**

A comparison of DSC's reported financial activity to its bank records revealed that, for 2006, reported receipts were overstated by \$54,740 and ending cash was similarly overstated. The Audit staff recommended that DSC amend its reports to correct the misstatement.

##### **Legal Standard**

**Contents of Reports.** Each report must disclose:

- The amount of cash on hand at the beginning and end of the reporting period;
- The total amount of receipts for the reporting period and for the calendar year;

- The total amount of disbursements for the reporting period and for the calendar year; and
- Certain transactions that require itemization on Schedule A (Itemized Receipts) or Schedule B (Itemized Disbursements). 2 U.S.C. §434(b)(1), (2), (3), (4), and (5).

### Facts and Analysis

The Audit staff reconciled reported financial activity to bank records for calendar year 2006 and noted a misstatement of receipts and ending cash. The following chart outlines the discrepancies.

2006 Activity			
	Reported	Bank Records	Discrepancy
Opening Cash Balance @ August 3, 2006	\$0	\$0	\$0
Receipts	\$511,528	\$456,788	\$54,740 Overstated
Disbursements	\$462,788	\$462,779	\$9 Overstated
Ending Cash Balance @ December 31, 2006	\$48,740	\$(5,991)	\$54,731 Overstated

The overstatement of receipts resulted from the following:

- Bank adjustments, e.g., reported contribution checks returned for non-sufficient funds \$ 49,350
- Contribution from BUILD PAC reported twice 5,000
- Reported loan from Candidate not supported by deposit 500
- Contribution amounts reported incorrectly (net) 90
- Unitemized receipts understated (300)
- Unexplained difference 100

Net overstatement of receipts \$ 54,740

The \$54,731 overstatement of ending cash on hand resulted primarily from the misstatement of receipts noted above.

At the exit conference, the Audit staff explained the misstatements and indicated that most of the receipts difference was due to bank adjustments that were not subsequently corrected in the reports. Schedules were provided to D&C's representative detailing these discrepancies. The representative explained that he didn't have access to bank statement information when preparing the reports. He agreed to review the schedules provided.

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### **Interim Audit Report Recommendation**

The Audit staff recommended that, within 30 calendar days of service of the interim report, DSC amend its reports to correct the misstatements noted above.

## **Finding 5. Disclosure of Contributions**

### **Summary**

Results of a review of all contributions received from individuals indicated that DSC did not adequately disclose the name and address of contributors or the date of receipt for individual contributions totaling \$46,150. The Audit staff recommended that DSC amend its reports to correct the disclosure of these contributions.

### **Legal Standard**

**A. Itemization Required for Contributions from Individuals.** An authorized candidate committee must itemize any contribution from an individual if it exceeds \$200 per election cycle, either by itself or when combined with other contributions from the same contributor. 2 U.S.C. §434(b)(3)(A).

**B. Election Cycle.** The election cycle begins on the first day following the date of the previous general election and ends on the date of the next general election. 11 CFR §100.3(b).

**C. Required Information for Contributions from Individuals.** For each itemized contribution from an individual, the committee must provide the following information:

- The contributor's full name and address (including zip code);
- The contributor's occupation and the name of his or her employer;
- The date of receipt (the date the committee received the contribution);
- The amount of the contribution; and
- The election cycle-to-date total of all contributions from the same individual. 2 U.S.C. §434(b)(3)(A) and 11 CFR §§100.12 and 100.3(a)(4).

### **Facts and Analysis**

Results of a review of contributions received from individuals required to be itemized indicated that DSC did not adequately disclose the name and address of contributors or the date of receipt for 38 contributions totaling \$46,150. Most of the discrepancies were due to the disclosure of an incorrect date of receipt. Although the Audit staff could not determine the source of the date used by DSC, in most instances the date reported was three to five days after the date on the deposit slip. Most of these errors occurred for contributions deposited during the month of October 2008.

At the exit conference, DSC was provided schedules detailing these discrepancies. The DSC representative agreed to review these schedules.

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### **Interim Audit Report Recommendation**

The Audit staff recommended that, within 30 calendar days of service of the interim report, DSC amend its report to correct the disclosure of these receipts on Schedule A (Itemized Receipts).

## **Finding 6. Failure to File 48-Hour Notices**

### **Summary**

DSC did not file 48-hour notices for 15 contributions totaling \$94,100 received prior to both the primary and general elections. Of this amount, \$84,000 was loans from the Candidate. The Audit staff recommended that DSC provide evidence that 48-hour notices were timely filed, that no notice was required, or submit any comments it considers relevant.

### **Legal Standard**

**Last-Minute Contributions (48-Hour Notice).** Campaign committees must file special notices regarding contributions of \$1,000 or more received less than 20 days but not more than 48 hours before any election in which the candidate is running. This rule applies to all types of contributions to any authorized committee of the candidate, including:

- Contributions from the candidate;
- Loans from the candidate and other non-bank sources; and
- Endorsements or guarantees of loans from the banks. 11 CFR §104.5(f).

### **Facts and Analysis**

The Audit staff reviewed 55 contributions, totaling \$177,551, which were greater than \$1,000 and received during the 48-hour notice filing period of both the primary and general elections. DSC did not file 48-hour notices for 15 contributions totaling \$94,100. Of this amount, six contributions totaling \$84,000 were loans from the Candidate.

At the exit conference, DSC was provided a schedule of the 48-hour notices not filed. The DSC representative stated that he would review these schedules.

### **Interim Audit Report Recommendation**

The Audit staff recommended that, within 30 calendar days of service of the interim report, DSC provide:

- Documentation to demonstrate that 48-hour notices were filed for the contributions in question; or
- Documentation establishing the contributions were not subject to 48-hour notification; and
- Any comments it considers relevant.

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## **Finding 7. Disclosure of Occupation and Name of Employer**

### **Summary**

DSC did not adequately disclose occupation and/or name of employer information for contributions from individuals totaling \$55,350. In addition, there was no evidence that "best efforts" to obtain, maintain and submit the information had been exercised. The Audit staff recommended that DSC demonstrate that it has exercised best efforts to obtain the necessary information or contact each contributor for which the information is lacking, submit evidence of such contact, and disclose any information received in amended reports.

### **Legal Standards**

**A. Required Information for Contributions from Individuals.** For each itemized contribution from an individual, the committee must provide the contributor's occupation and the name of his or her employer. 2 U.S.C. §431(13) and 11 CFR §100.12.

**B. Best Efforts Ensures Compliance.** When the treasurer of a political committee shows that the committee used best efforts (see below) to obtain, maintain, and submit the information required by the Act, the committee's reports and records will be considered in compliance with the Act. 2 U.S.C. §432(h)(2)(i).

**C. Definition of Best Efforts.** The treasurer and the committee will be considered to have used "best efforts" if the committee satisfied all of the following criteria:

- All written solicitations for contributions included:
  - A clear request for the contributor's full name, mailing address, occupation, and name of employer; and
  - The statement that such reporting is required by Federal law.
- Within 30 days after the receipt of the contribution, the treasurer made at least one effort to obtain the missing information, in either a written request or a documented oral request.
- The treasurer reported any contributor information that, although not initially provided by the contributor, was obtained in a follow-up communication or was contained in the committee's records or in prior reports that the committee filed during the same two-year election cycle. 11 CFR §104.7(b).

### **Facts and Analysis**

The Audit staff reviewed all reported contributions from individuals to determine if the necessary contributor information was disclosed. The review indicated that DSC did not adequately disclose the occupation and/or name of employer for 44 contributions totaling \$55,350. For \$32,100 of these items, DSC disclosed an occupation such as developer or investor with no name of employer. In addition, for \$19,250, DSC disclosed that best efforts had been exercised.

Although requested, DSC did not provide copies of solicitation materials or a description of their best efforts procedures. In addition, the records provided to the Audit staff did

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not contain any follow-up requests for missing contributor information. As a result, DSC does not appear to have made "best efforts" to obtain, maintain and report occupation and name of employer information.

At the exit conference, DSC was provided schedules of the contributions requiring additional disclosure information. The DSC representative stated that these schedules would be reviewed and any comments regarding DSC's best efforts procedures would be submitted in writing.

#### **Interim Audit Report Recommendation**

The Audit staff recommended that, within 30 calendar days of service of the interim report, DSC take the following action:

- Provide documentation such as phone logs, returned contributor letters, completed contributor contact information sheets or other materials which demonstrate that best efforts were made to obtain, maintain, and submit the required disclosure information; or
- Absent such a demonstration, make an effort to contact those individuals for whom required information is missing or incomplete, provide documentation of such contacts (such as copies of letters to the contributors and/or phone logs), and amend its reports to disclose any information obtained from those contacts.

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